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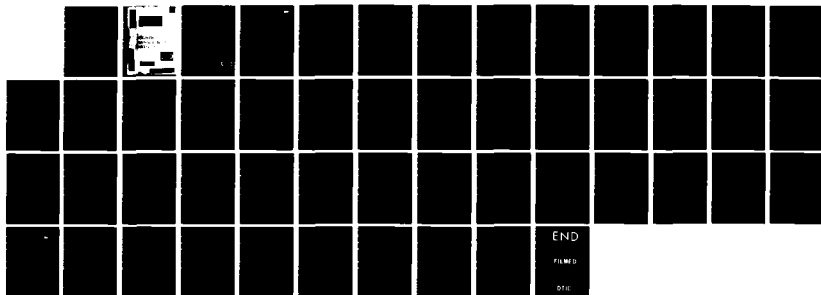
TEST OF PROPOSED CHANGES IN THE IMPACT AID PROGRAM(U)  
LOGISTICS MANAGEMENT INST BETHESDA MD  
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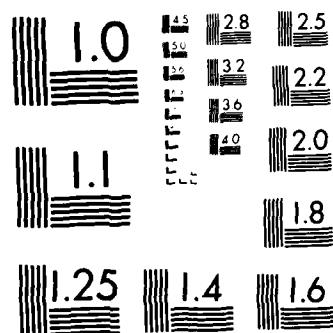
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TEST OF PROPOSED CHANGES  
IN THE IMPACT AID PROGRAM

February 1985

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## Executive Summary

### TEST OF PROPOSED CHANGES IN THE IMPACT AID PROGRAM

In April 1984 we proposed these changes in the Impact Aid program:<sup>1</sup>

- Eliminating Impact Aid payments for low-rent-housing children and for Category B dependents of Federal civilian employees;
- Raising the entitlement weights for Category B military dependents;
- Revising the method for computing the Local Contribution Rate (LCR); and
- Changing the method for allocating Impact Aid funds when not enough money is available to pay districts at the full-entitlement level.

We have now tested the proposed changes by comparing payments that were made to school districts in fiscal year 1982 with payments that would have been made under the revised methods. This is how the test results measure up against the improvement objectives stated in the April 1984 report:

Objective #1: Provide more Impact Aid funds or an equitable share of available funds to school districts that serve military dependents.

This objective is achieved substantially by the changes proposed.

- Sixty-eight percent of the military dependents are in districts that would receive higher payments.
- Thirty-two percent are in districts that would receive either lower payments or none at all. In most of these districts, military dependents represent less than five percent of total enrollment. Of the districts that lose funds and have high proportions of military dependents, some might be eligible for supplementary payments.

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<sup>1</sup>Isidore M. Greenberg, Proposal to Revise the Federal Impact Aid Program, Task ML326 (Washington, D.C.: Logistics Management Institute, April 1984).

Objective #2: Improve the method used to allocate Impact Aid when funds are short.

This objective is achieved by the proposed absorption-rate method. The sharp distinction between payments to Super districts and payments to regular districts is replaced by a method that favors highly impacted districts on a smooth, graduated scale. To protect payments to heavily impacted districts when funds are short, payments to very lightly impacted districts are either reduced substantially or eliminated entirely.

Objective #3: Simplify the payment system.

This objective is achieved by:

- Simplifying the computation of district LCRs;
- Reducing the number of types of federally connected children from 15 to 7; and
- Providing an efficient method for computing payments to each district for several alternative levels of funding.

We recommend that the Department of Defense seek adoption of the proposed changes in the Impact Aid program.

Mustering support for these changes will be difficult, because more school districts will lose funds than will gain, and many districts will receive nothing at all. In the past, Congress has favored solutions that spread the available funds among many districts and has opposed eliminating payments for any of the currently eligible types of federally connected children.

It is feasible to adopt parts of the package of changes rather than the whole package. We recommend that compromise solutions be tested before adoption.

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## 1. INTRODUCTION

Our April 1984 report "Proposal to Revise the Federal Impact Aid Program" recommended the following changes:<sup>1</sup>

- Eliminate Impact Aid payments for low-rent-housing Category A and B children and for Category B dependents of Federal civilian employees.<sup>2</sup>
- Raise the entitlement weights assigned to Category B military dependents and lower the weight assigned to Category A dependents of Federal civilian employees.
- Revise the method for computing Local Contribution Rates (LCRs) to simplify the process and to reduce excessive LCRs.
- Revise the method for allocating Impact Aid funds when the funds available for distribution to school districts is lower than the amount required at the full-entitlement level.

The objectives of the proposed changes in that report were to:

- Provide more Impact Aid funds or an equitable share of available funds to school districts serving military dependents;
- Improve the formulas used to allocate Impact Aid funds when funds are short; and
- Simplify a payment system that has become overly complicated.

In this report, we will examine the results of the test to determine whether the proposed payment system meets these three objectives.

The April 1984 report and the test deal only with payments made under Sections 3(a) and 3(b) of Public Law (P.L.) 81-874. Some school districts receive additional payments authorized by other sections of P.L. 81-874 and by P.L. 81-815.

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<sup>1</sup>The Executive Summary of the April 1984 report is included as Appendix A to this new report. Those interested in a more detailed description of the proposed changes and their justification should read the entire April 1984 report.

<sup>2</sup>The parents of Category A children live and work on Federal property. The parents of Category B children live or work on Federal property, but not both.



## TEST DESIGN

The test evaluated the proposed Logistics Management Institute (LMI) changes by comparing the Section 3(a) and 3(b) payments made to districts in fiscal years 1981, 1982, and 1983 to the payments they would have received if the LMI system had been in effect in these three years. This report summarizes the comparisons at State and national level. The comparisons for each individual district have been provided to the Department of Defense (DoD).

Fiscal year 1982 (FY82) was selected for intensive analysis because it was the most recent year for which all necessary data were available in the Department of Education (DoED) data files.

DoED payments were compared to proposed LMI payments for three different funding options in FY82:

- Full entitlement;
- Actual funding; and
- Less than actual funding.

The LMI payments computed for a district reflect the combined impact of all of the proposed LMI changes to the payment system. One of the proposed changes involves changing (and, in most cases, reducing) the LCR for each district. To isolate the effect of the LCR change, LMI payments were computed two ways:

- Applying all changes proposed by LMI, including new LCRs (Case #1); and
- Applying all LMI changes, except the change in LCRs (Case #2). In Case #2 we use the DoED LCRs.

Table 1-1 shows the funding levels used in the test.

This report concentrates on Cases #1 and #2, the allocation of the \$420 million actually spent in FY82.

TABLE 1-1. FUNDING LEVELS - FY82

PAYMENTS	FUNDING LEVELS (\$ MILLIONS)		
	Full Entitlement	Actual Expenditures	Reduced Expenditures <sup>a</sup>
DoED	\$1,151	\$420	\$358
<u>LMI</u>			
Using LMI LCRs	\$546	\$420 (Case #1)	\$358
Using DoED ECRs	\$657	\$420 (Case #2)	\$358

<sup>a</sup>\$420 million less the amount expended by DoED for low-rent-housing students and Category B civilian students equals the \$358 million reduced-expenditure level.

The data in the report cover all 50 States and the District of Columbia but exclude Puerto Rico, Guam, and the Virgin Islands.<sup>3</sup>

<sup>3</sup>In FY82, these three regions received \$4 million in Section 3(a) and 3(b) payments.

## 2. INDEPENDENT EFFECT OF EACH CHANGE TO THE PAYMENT SYSTEM

This chapter discusses how each of the changes proposed by LMI affects the payments received by districts. Chapter 3 describes the combined effect of the changes.

### ELIMINATION OF IMPACT AID FOR SOME TYPES OF STUDENTS

We recommended that the following types of federally connected students be dropped from the Impact Aid program:

- Civilian low-rent housing, Categories A and B; and
- Federal civilian employee dependents, Category B.

In FY82, school districts received \$61 million for these students -- \$27 million for 740,000 low-rent-housing children and \$34 million for 750,000 Category B dependents of Federal employees. The average per-pupil payment was only about \$40.

Most districts that educate military dependents also educate Category B civilian dependents,<sup>1</sup> and some also educate low-rent-housing children. Therefore, dropping these types of children reduces the Impact Aid entitlement for most districts that educate military dependents. Other changes proposed by LMI help offset this loss in funds.

### ENTITLEMENT WEIGHTS

Table 2-1 compares the authorized entitlement weights to those recommended by LMI for children retained in the Impact Aid program.<sup>2</sup> We recommended restoring the authorized entitlement weights for Category B military

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<sup>1</sup>About one-half of the Federal civil service workers are employed by DoD activities.

<sup>2</sup>Weights would no longer be needed for low-rent-housing children and for Category B dependents of Federal civilian employees.

dependents to their FY81 level of 0.5 (0.75 for special education). We also recommended reducing the weights for Category A Federal civilian dependents to 0.7.

TABLE 2-1. ENTITLEMENT WEIGHTS FOR RETAINED STUDENTS

	AUTHORIZED			LMI PROPOSED
	FY81	FY82	FY83-84	
<u>Military</u>				
Category A	1.0	1.0	1.0	1.0
Category A - SPED <sup>a</sup>	1.5	1.5	1.5	1.5
Category B	0.5	0.333 <sup>b</sup>	0.167 <sup>b</sup>	0.5
Category B - SPED <sup>a</sup>	0.75	0.5 <sup>b</sup>	0.25 <sup>b</sup>	0.75
<u>Indian</u>				
Category A	1.25	1.25	1.25	1.25
Category A - SPED <sup>a</sup>	1.875	1.875	1.875	1.875
<u>Civilian</u>				
Category A	0.9	0.9	0.9	0.7
Category A - Super District	1.0	1.0	1.0	0.7

<sup>a</sup>Special Education.

<sup>b</sup>Starting in FY82, Congress modified the FY81 weights for low-rent-housing and Category B students by establishing maximum allowable payment levels. In FY82 the effective weight for Category B military dependents was two-thirds of the FY81 weight; in FY83-84 the effective weight was one-third of the FY81 weight.

Only 7,000 children would be affected by the weight reduction for Category A civilians, but the proposed increase in the weights for Category B military dependents would affect payments for 310,000 children. The April 1984 LMI report provided the reasons for retaining Category B military dependents in the Impact Aid program and raising the weights for these children. About 60 percent of the military dependents are Category B, and about 40 percent are Category A.

The entitlement weights for Category A military dependents and for Indian children would not change.

#### LOCAL CONTRIBUTION RATE

The LCR is a key element in the process of computing Impact Aid payments. DoED multiplies the district LCR by the number of federally connected students in the district and the entitlement weight for each type of student. Prorating factors are then applied to reduce full entitlement to actual payments that fit within the total funds appropriated by Congress.

Districts now have the option of selecting one of three different methods for computing their LCRs. Districts select the method that results in the highest LCR for their districts. LMI recommended changing the method for computing LCRs as shown in Table 2-2.

TABLE 2-2. LOCAL CONTRIBUTION RATE

CURRENT OPTIONS	LMI PROPOSED OPTIONS
1/2 National Average Per-Pupil Cost	Eliminate
1/2 State Average Per-Pupil Cost	1/2 State Average Per-Pupil Cost, Less Federal Contribution
Local Per-Pupil Expenditures in Comparable Districts	Eliminate
	Average Per-Pupil Expenditures from Local Revenue Sources in Applicant's State

The LMI LCRs for each district were computed from data published by the National Center for Educational Statistics in the Digest of Education

Statistics.<sup>3</sup> It was assumed that all of the districts within a State would select the option that provides the highest LCR. Each district within a State would therefore have the same LCR. In about one-half of the States, the districts would base their LCRs on "1/2 of the State Average Per-Pupil Cost, Less Federal Contribution." The districts in the other States would base their LCRs on "Average Per-Pupil Expenditures from Local Revenue in the Applicant's Own State." This second option would be selected by districts in States that provide less in-State aid than the amount raised from local tax revenues (e.g., Connecticut).

The LCR change proposed by LMI would reduce full entitlement by 17 percent.<sup>4</sup> The table in Appendix B shows the LCR reductions by State. Forty-one States experience LCR reductions that range from 1 to 43 percent, and ten (including the District of Columbia) have LCR increases that range from 1 to 66 percent. LCR changes for each district are in printouts provided to DoD.

The LMI method for computing LCRs reduces LCRs substantially in the following types of districts:

- Those that have educational costs below the national average but currently select one-half of the national average as their LCR; and
- Those that currently use the "comparable district" method for determining their LCR.

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<sup>3</sup>For FY82 LCRs, we used the table on "Expenditure Per Pupil in Average Daily Attendance in Public Elementary and Secondary Schools, by State: 1980-81" and the table on "Revenue and Nonrevenue Receipts of Public Elementary and Secondary Schools by Source and by State: 1980-81." By law, LCRs are calculated on the basis of educational costs two years preceding the year for which Impact Aid payments are made.

<sup>4</sup>To measure the independent effect of changing the LCRs, we computed LMI full entitlement for FY82 using LMI LCRs for each district (Case #1 -- \$545.7 million) and then by using the original DoED LCRs (Case #2 -- \$657.1 million). The switch to LMI LCRs reduced full entitlement by 17 percent for the United States as a whole. As discussed in Chapter 3, it is desirable to reduce full entitlement to a realistic amount that is closer to actual funding levels.

When available funds are not sufficient to make payments at the full-entitlement level, the LMI payment system tends to close the gap by dropping low-impact districts and concentrating the funds into districts heavily impacted with federally connected students.

The LMI payment to a district reflects the combined effect of several changes to the payment system: elimination of some types of students; higher weights for Category B military dependents; a change in LCR computation method; and the new absorption-rate mechanism. Table 3-5 describes the characteristics that determine whether a district gains or loses as a result of the LMI payment system. Losing districts tend to have one or more of the characteristics shown in the "Losers" column. Winning districts tend to have one or more of the characteristics shown in the "Gainers" column. Many districts have both losing and gaining characteristics. The test was needed to quantify the combined effect of all changes on each district.

TABLE 3-5. CHARACTERISTICS OF DISTRICTS THAT GAIN OR LOSE UNDER LMI PAYMENT SYSTEM

CHARACTERISTIC	LOSERS	GAINERS
Federal ADA <sup>a</sup> as a Percentage of Total ADA	<u>Low</u> Case #1 - Below 5% Case #2 - Below 10%	<u>Medium and High</u> Case #1 - Above 5% Case #2 - Above 10%
Type of Federal Students	Primarily Low-Rent Housing and Category B Civilian	Primarily Indian and Military, Including Category B Military
Local Contribution Rate	LCR Reduced Heavily by LMI Method	LCR Reduced Moderately or Increased

<sup>a</sup>Military, Indian, and Category A Federal civilian students, unweighted.

### District Comparisons

Computer printouts have been provided to DoD that compare the Impact Aid payments each district would have received under the LMI payment system with the payments actually received by these districts. Table 3-4 summarizes the changes in payments for the 2,193 districts that received Section 3(a) and 3(b) payments in FY82.

TABLE 3-4. EFFECT OF LMI PAYMENTS ON DISTRICTS

FY82 - \$420 Million

	NUMBER OF DISTRICTS	
	LMI LCRs (Case #1)	DoED LCRs (Case #2)
Received DoED Payments	2,193	2,193
<u>LMI Payments</u>		
<u>Losing Districts</u>	<u>1,663</u>	<u>1,697</u>
Dropped	(1,178)	(1,396)
Retained but Paid Less	(485)	(301)
<u>Gaining Districts</u>	<u>530</u>	<u>496</u>

In FY82, about 75 percent of the 2,193 districts would have received less under the LMI payment system than they actually received. Most of the losing districts would have received zero payments;<sup>6</sup> the remainder of the losing districts would have been retained but would have received lower payments. About 25 percent of the districts would have received higher payments.

<sup>6</sup>Case #2 eliminates more districts because it is based on a higher absorption rate than Case #1. In Case #2, a 3.78-percent absorption rate is required to reduce the \$657 million full-entitlement level to actual payments of \$420 million. In Case #1, an absorption rate of 1.75 percent is required to reduce the \$546 million full-entitlement level to actual payments of \$420 million.



During the test, we developed the procedures for performing, in a few hours, the following operations:

- Locate the precise absorption rate necessary to achieve a given funding level; and
- Print out the fund allocation by district.

The absorption-rate mechanism would enable DoED to compute, in one day, how several different funding levels proposed by the Executive Branch or Congress would affect payments to individual districts.

#### LMI PAYMENTS COMPARED TO DoED PAYMENTS

For each State and district, we compared the actual payments made by DoED to the payments that would have been made on the basis of the LMI payment system. Again, the results are for FY82 for two LMI payment cases:<sup>4</sup>

- Case #1 -- allocation of \$420 million using LMI LCRs; and
- Case #2 -- allocation of \$420 million using DoED LCRs.

#### State Comparisons

Appendix C summarizes the payment changes by State. Using the LMI payment system would cause major changes. For example, in Case #1, 20 States would suffer reductions of 5 percent or more, and 14 of these losing States would suffer reductions ranging from 25 to 100 percent. Seventeen States would experience payment increases of 5 percent or more. There are also substantial differences between State results for Case #1 and Case #2.

The State totals have limited utility, because all losing States contain some winning districts, and all States that gain as a result of the LMI payment system contain some districts that lose.<sup>5</sup>

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<sup>4</sup>Cases #3 and #4 allocate \$358 million using LMI LCRs (Case #3) and DoED LCRs (Case #4).

<sup>5</sup>There are two exceptions, namely Hawaii and the District of Columbia, each of which has a single district.

rate needed to match total district payments to a given funding level or to alternative funding levels for the Impact Aid program. Table 3-3 demonstrates that this can be done. During the test, we located the absorption rate for two different funding levels, starting with two different full-entitlement assumptions.

TABLE 3-3. ABSORPTION RATE REQUIRED TO REDUCE FULL ENTITLEMENT TO SELECTED FUNDING LEVELS - FY82

CASE	FULL ENTITLEMENT	FUNDING LEVEL	ABSORPTION RATE
#1	\$545,725,048 <sup>a</sup>	\$419,926,698 <sup>c</sup>	1.75471%
#2	\$657,115,230 <sup>b</sup>	\$419,926,698 <sup>c</sup>	3.78486%
#3	\$545,725,048 <sup>a</sup>	\$358,308,365 <sup>d</sup>	3.46342%
#4	\$657,115,230 <sup>b</sup>	\$358,308,365 <sup>d</sup>	5.78173%

<sup>a</sup>LMI full entitlement using LMI LCRs.

<sup>b</sup>LMI full entitlement using DoED LCRs.

<sup>c</sup>Actual FY82 funding level.

<sup>d</sup>Assumed reduced funding level for FY82.

As shown in Table 3-3, we applied a 1.75-percent absorption rate in Case #1 to close the gap between a full-entitlement level of \$546 million and actual funding of \$420 million. We estimate that, if the LMI payment system were to be in effect in FY85, an absorption rate of only 0.8 percent would be required to close the gap between the LMI full-entitlement level of \$740 million and actual funding of \$643 million. About 1,300 to 1,400<sup>3</sup> districts would receive payment. (At the 1.75-percent absorption rate used in the test for FY82, only 915 districts would have received payment.)

<sup>3</sup>The 1,400 estimate assumes that the \$5,000-minimum-payment rule is not applied in FY85.

- All remaining districts are required to absorb 1 percent of their total ADA without payment.

TABLE 3-2. LMI PAYMENTS BY ABSORPTION RATE - FY82

ABSORPTION <sup>a</sup> RATE	LMI PAYMENT (\$ MILLIONS)		NUMBER OF DISTRICTS PAID	
	LMI LCRs (Case #1)	DoED LCRs (Case #2)	LMI LCRs (Case #1)	DoED LCRs (Case #2)
0% (Full Entitlement)	\$546	\$657	2,175	2,266
1%	\$457	\$552	1,132	1,145
2%	\$409	\$494	976	982
3%	\$373	\$450	866	874
4%	\$342	\$412	769	778
5%	\$317	\$381	709	716
6%	\$294	\$353	663	672

<sup>a</sup>Absorption Rate x Total District ADA = Number of Weighted Federal Students Absorbed by a District. No payment is made for absorbed students.

As the absorption rate is raised above 1 percent, payments continue to decrease and more districts are eliminated, but the rate of reduction slows.

As shown in Table 3-2, the absorption-rate mechanism eliminates fewer districts in achieving a given funding level when the full entitlement starting point is lower. For example, in Case #1, a 1-percent absorption rate reduces funding to \$457 million and pays 1,132 districts. In Case #2, which starts with a higher full entitlement, a 3-percent absorption rate is required to reduce funding to about the same amount. The 3-percent absorption rate reduces the number of districts paid to 874, as compared to 1,132 districts paid in Case #1 for about the same funding level.

Table 3-2 demonstrates that it is feasible to determine how district payments are affected by various absorption rates. The managers of the Impact Aid program would also need the capability of finding the precise absorption

We believe the Impact Aid program is improved by reducing full entitlement to a realistic amount close to actual funding levels. The gap between LMI Case #1 full entitlement and actual funding was 23 percent in FY82, was 20 percent in FY84, and is estimated to be only 13 percent in FY85.<sup>1</sup> The next section of this report will describe how the absorption-rate mechanism would function in closing the gap between full entitlement and actual funding.

#### LMI PAYMENTS BY ABSORPTION RATE

Although it would be desirable to fund the Impact Aid program at the full-entitlement level, the absorption-rate mechanism can adjust payments to any funding level below full entitlement. Table 3-2 shows how absorption rates ranging from 1 to 6 percent would affect payment levels in FY82 and the number of districts eligible for payment. The absorption rates are applied to two full-entitlement levels:

- Case #1 -- \$546 million; and
- Case #2 -- \$657 million.

Table 3-2 shows that in Case #1 the imposition of a 1-percent absorption rate would decrease the payment level from \$546 to \$457 million (a 16-percent reduction) and reduce the number of districts eligible for payment from 2,175 to 1,132 (a 48-percent reduction). About the same percentage reduction occurs with a 1-percent absorption rate in the Case #2 example, which starts with a \$657 million full entitlement. A 1-percent absorption rate has such a powerful effect in reducing payments below full entitlement because:

- Districts with a weighted Federal ADA of 1 percent or less than their total ADA receive no payment;
- Districts that earn a payment of less than \$5,000 after application of the absorption rate receive no payment;<sup>2</sup> and

<sup>1</sup>In FY81, LMI Case #1 full entitlement (\$490 million) was lower than actual funding (\$606 million).

<sup>2</sup>The \$5,000-minimum-payment rule was in effect during FY82-84 and was therefore applied for these years to calculate LMI payments.

TABLE 3-1. DoED AND LMI FULL ENTITLEMENT COMPARED  
TO ACTUAL FUNDING

(\$ Millions)

	FY81	FY82	FY84
<u>Full Entitlement</u>			
DoED	\$1,263	\$1,151	\$987
LMI <sup>a</sup>			
Case #1 (LMI LCRs)	490	546	672 <sup>b</sup>
Case #2 (DoED LCRs)	591	657	711 <sup>b</sup>
Actual Funding	\$606	\$420	\$535
<u>Actual as a % of:</u>			
DoED Full Entitlement	48%	37%	54%
LMI Full Entitlement			
Case #1	124%	77%	80% <sup>b</sup>
Case #2	103%	64%	66% <sup>b</sup>

<sup>a</sup>LMI full entitlement is most likely understated by about \$5 million, because the DoED data base omits districts that do not meet the legal 3-percent eligibility criterion. These districts would be permitted to apply under the LMI proposal, although most would not receive payment if the actual funding level required the use of an absorption rate.

<sup>b</sup>Estimated.

The changes proposed by LMI would reduce full entitlement substantially below the DoED levels, especially if LMI LCRs were to be used (Case #1). For example, in FY84 LMI full entitlement for Case #1 is \$672 million, as compared to \$987 million for DoD full entitlement. The reduction in full entitlement is achieved by dropping low-rent-housing students and Category B Federal-employee dependents from the Impact Aid program and by using the lower LCRs proposed by LMI. The LMI full entitlement for Case #2 is higher than for Case #1, because Case #2 uses the higher DoED LCRs.

### 3. TEST RESULTS

This chapter describes the combined effect of the proposed changes to the Impact Aid program by comparing payments based on the LMI proposals to actual payments made by DoED. LMI payments are shown for two cases:

- Case #1 -- Using LMI LCRs, and all other proposed changes to the payment system; and
- Case #2 -- Using DoED LCRs, but applying all other proposed changes to the payment system.

#### FULL ENTITLEMENT

Full entitlement represents the Section 3(a) and 3(b) payments that districts would receive if Congress appropriated enough money to pay the full amount permitted by the authorizing legislation. Historically, Congress has appropriated much less than is required to fund full entitlement. A large gap between full entitlement and actual funding causes districts to feel they are receiving much less than they deserve. In this atmosphere of discontent, any formula for allocating available funds is sure to be controversial.

Table 3-1 compares the DoED full entitlement to the full entitlement derived from the application of the LMI proposals.

In FY81, DoED full entitlement was \$1,263 million, as compared to actual funding of \$606 million. Inflation would normally have increased full entitlement to about \$1,700 million by FY84. However, Congress reduced the effective entitlement weights for Category B students each year in FY82, FY83, and FY84 by establishing maximum allowable payment levels. These changes more than offset inflation, but full entitlement in FY84 was still nearly twice as large as actual funding (\$987 million compared to \$535 million).

TABLE 2-3. APPLICATION OF ABSORPTION RATE

Assuming: Absorption Rate of 2%; LCR of \$1,500

COMPUTATION STEPS	DISTRICTS		
	X	Y	Z
Total ADA	10,000	10,000	10,000
Unweighted Federal ADA	360	200	1,500
Weighted Federal ADA	180	250	1,000
Absorbed (2% x Total ADA)	200	200	200
Weighted Federal ADA Eligible for Payment	0	50	800
Payment (LCR x Eligible)	0	\$75,000	\$1,200,000

- Paying low-impact districts a small portion of their full entitlement;  
and
- Imposing some penalty on all districts, even high-impact districts.

FIGURE 2-2. LMI PAYMENTS AS A PERCENTAGE OF FULL ENTITLEMENT  
CALIFORNIA, FY82

Assumed Absorption Rate = 1.75%

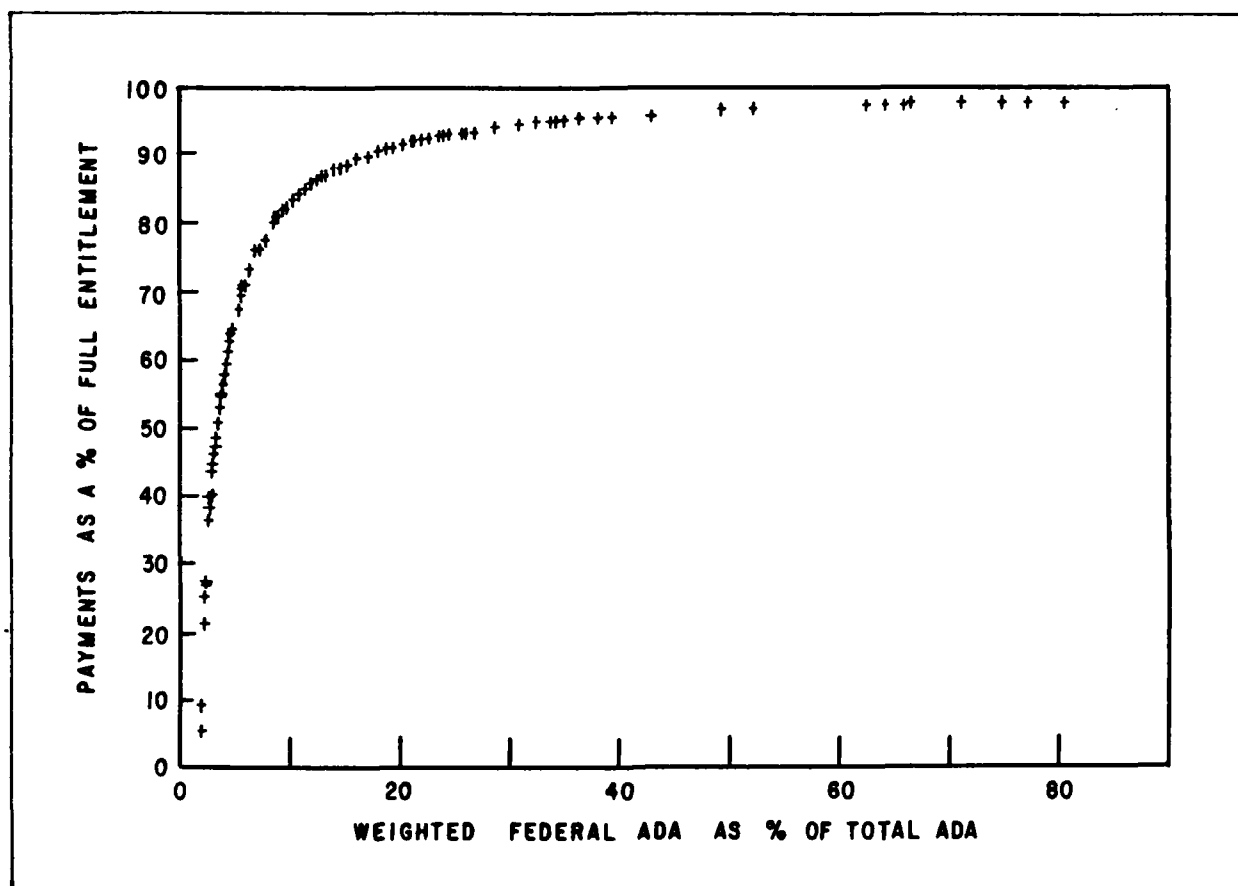


Table 2-3 shows the application of the absorption rate to three hypothetical districts, each of which has a total ADA of 10,000 but different numbers of federally connected students.

This concludes our description of the individual parts of the LMI payment mechanism. The next chapter of the report will show the combined effect of the LMI proposals on payments to districts.



The weights used in computing weighted Federal ADA are those recommended in the April 1984 report:<sup>7</sup>

Federal Civilian Category A	0.70
Indian	1.25
Indian - Special Education (SPED)	1.875
Military Category A	1.00
Military Category A - SPED	1.50
Military Category B <sup>8</sup>	0.50
Military Category B - SPED	0.75

To illustrate, a district with 40 Category A military dependents and 40 Category B military dependents and no other federally connected children would have a weighted Federal ADA of 60. In a district with a total ADA of 1,000, the weighted Federal ADA would be 6 percent of total ADA.

Figure 2-2 shows how an absorption rate of 1.75 percent<sup>9</sup> would have affected payments to California districts in FY82. In this graph, payments are expressed as a percentage of full entitlement. Payments vary as a function of the level of impact, shown as "Weighted Federal ADA as % of Total ADA." Note that the curve in Figure 2-2 has the same shape as the curve in Figure 2-1 for the auto insurance example. Raising the absorption rate from 1.75 to 3.5 percent would move the curve to the right, but the shape of the curve would be the same.

Ideally, all districts should be paid at 100 percent of full entitlement. If funds are not available to pay all districts at the full-entitlement level, the absorption mechanism closes the gap in funding by:

- Making zero payments to districts having a weighted Federal ADA percentage at or below the absorption rate;

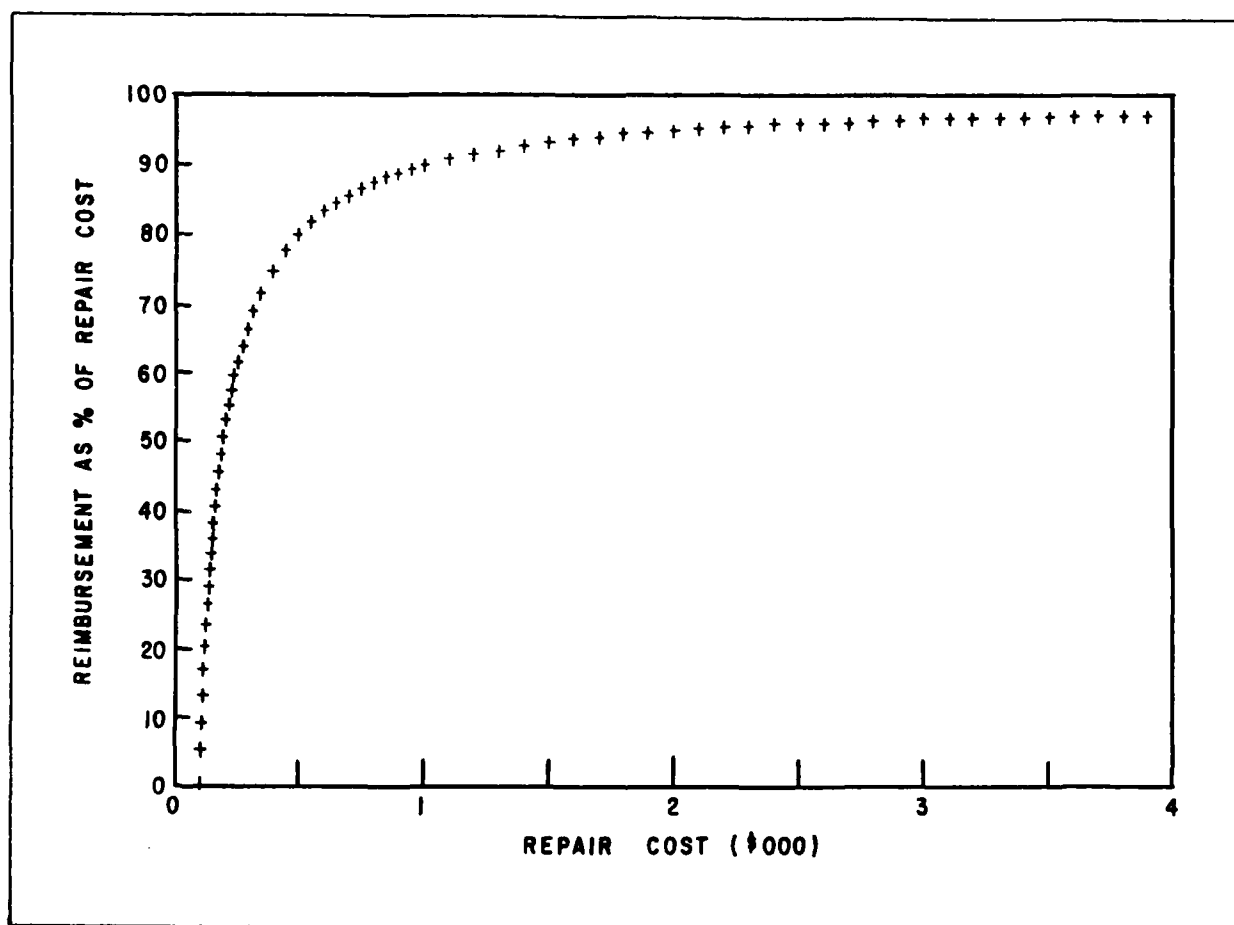
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<sup>7</sup>Low-rent-housing children and Category B dependents of Federal employees are not included in the weighted Federal ADA count because, under LMI's proposal, they would be dropped from the Impact Aid program.

<sup>8</sup>Includes former military low-rent-housing Category A (3A2 LRH).

<sup>9</sup>This absorption rate was used in the test.

FIGURE 2-1. INSURANCE REIMBURSEMENTS FOR AUTO COLLISION INSURANCE  
WITH \$100 DEDUCTIBLE



This new method favors more heavily impacted districts on a continuous, graduated scale and abandons the current 3-percent eligibility rule<sup>6</sup> and the Super-district concept. Furthermore, the new method computes level of impact by weighting the Federal students by the entitlement weights instead of using a raw count of Federal students. The level of impact for a district is based on weighted Federal ADA as a percentage of total ADA.

<sup>6</sup>Currently, districts whose Federal-student count is less than 3 percent of their total ADA are not eligible for Section 3 Impact Aid payments, unless they have 400 or more federally connected students.

payments at the full-entitlement level. When funds are not sufficient to make payments at the full-entitlement level, we recommend applying a new method, called the absorption-rate method, that:

- Eliminates the sharp distinction between Super districts and regular districts;
- Requires all districts to absorb some federally connected children without payment, on the basis of a percentage of their total (Federal and non-Federal) average daily attendance (ADA); and
- Permits the absorption rate to vary each year in relation to the gap between full entitlement and funds available for allocation.

The proposed absorption-rate method is based on the same principle used in auto collision insurance. The insurance premiums of "full coverage" are too high for most motorists, so they buy insurance with a deductible provision of \$100 or \$200. If the deductible is \$100, the insurance company deducts a flat \$100 from the total repair cost in reimbursing the motorist. This means that a motorist with a repair bill of \$100 or less receives nothing; a motorist with a repair bill of \$200 receives 50 percent of the full repair cost; a motorist with a repair bill of \$1,000 receives 90 percent of the repair cost. Figure 2-1 plots the payment curve.

The absorption-rate mechanism uses the concept of an insurance deductible. If sufficient funds are available to pay all districts at the full-entitlement level, the absorption rate is zero, which means that no deductible is applied. If funds available are insufficient, an absorption rate is applied to reduce district payments to match the total funds appropriated by Congress. The absorption rate will vary each year, because the gap between full entitlement and actual funding fluctuates annually.

The LMI method increases the LCRs for districts in States that have educational costs above the national average and rely on locally raised revenue for more than 50 percent of the per-pupil cost.

Although the LMI method tends to reduce LCRs significantly, it is only one of several changes we propose to the payment system. The combined effect of all of the LMI changes often increases the payments to districts that suffer an LCR reduction.

#### ELIGIBILITY AND ABSORPTION RULES

For many years, the Impact Aid funds available for allocation to districts have been substantially less than the amount required to make payments at the full-entitlement level. Congress has been establishing the priority system each year for allocating the available funds. Starting in FY82, the pattern in per-pupil payments has been:

- Highest priority for Category A students in Super A districts;<sup>5</sup>
- Second-highest priority for Category A students in regular districts;
- Low priority for Category A low-rent-housing students; and
- Token payments for Category B students.

The current allocation method creates a large difference in the per-pupil payments received by Super A districts as compared to regular districts and in the payments received for Category A students as compared to payments for Category B students. The prorating system negates the entitlement weights used in computing full entitlement.

Adopting the LMI recommendations for eliminating the eligibility of some types of students and for revising the LCR computation method would reduce full entitlement to a more affordable amount. It would be desirable to make

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<sup>5</sup> Districts in which the number of Category A students is 20 percent or more of the total Federal and non-Federal students in the district.

## DISTRICTS WITH MILITARY DEPENDENTS

One of the objectives of the proposed changes to the Impact Aid program is to provide more Impact Aid funds or an equitable share of available funds to school districts serving military dependents. This section of the report examines whether this objective is met by the proposed changes.

Table 3-6 shows that the proposed changes would have increased the proportion of total Impact Aid funds allocated for military dependents and sharply decreased the funds allocated for low-rent-housing and Federal civilian students. In Case #1, the decrease in funds for low-rent-housing students and for Category B Federal civilian employee dependents is shifted to Category B military dependents. The percentage for Category A military dependents remains unchanged. The percentage for total military dependents is increased from 54 to 69 percent. The proportion allocated to Indian students remains at 30 percent.

TABLE 3-6. PERCENTAGE OF IMPACT AID FUNDS BY TYPE OF STUDENT:  
DoED PAYMENTS COMPARED TO LMI PAYMENTS

FY82 - \$420 Million

	DoED PAYMENTS	LMI PAYMENTS	
		LMI LCRs (Case #1)	DoED LCRs (Case #2)
<u>Federal Civilian</u>	<u>10%</u>	<u>1%</u>	<u>1%</u>
Category A	(2)	(1)	(1)
Category B	(8)	(0)	(0)
<u>Low-Rent-Housing</u>	<u>6%</u>	<u>0%</u>	<u>0%</u>
Category A	(1)	(0)	(0)
Category B	(5)	(0)	(0)
<u>Indian - Category A</u>	<u>30%</u>	<u>30%</u>	<u>36%</u>
<u>Military</u>	<u>54%</u>	<u>69%</u>	<u>63%</u>
Category A	(48)	(48)	(45)
Category B	(6)	(21)	(18)
TOTAL	100%	100%	100%

In Case #2, the proportion allocated to Indian students rises from 30 to 36 percent, while the military drops from 69 to 63 percent. Case #2 is more favorable to Indian students. Two factors cause Case #2 to be more favorable to Indian students than Case #1:

- The DoED LCRs applied in Case #2 tend to help districts educating Indian children. Many of these districts use the "Comparable" method to compute their LCRs -- a method not permitted in Case #1.
- The higher absorption rate applied in Case #2 hurts military districts more than it hurts Indian districts. Indian districts tend to have a higher proportion of federally connected students; therefore, they are not hurt as much by the higher absorption rate.

The LMI payment system increases the proportion of funds allocated for military dependents. However, most districts that educate military dependents also contain Category B civilian students, and some also contain low-rent-housing and Indian students. The elimination of funds for Category B civilian and low-rent-housing students cuts off some of the funds previously received by districts educating military children. It is therefore necessary to examine how the LMI changes would affect the total Impact Aid funds received by districts educating military children.

Table 3-7 summarizes the effect on districts with military dependents.

TABLE 3-7. EFFECT OF LMI PAYMENTS ON DISTRICTS  
WITH SOME MILITARY DEPENDENTS

FY82 - \$420 Million

	NUMBER OF DISTRICTS	
	LMI LCRs (Case #1)	DoED LCRs (Case #2)
Received DoED Payments	1,666	1,666
<u>LMI Payments</u>		
<u>Losing Districts</u>	<u>1,309</u>	<u>1,396</u>
Dropped	(1,024)	(1,215)
Retained but Paid Less	(285)	(181)
<u>Gaining Districts</u>	<u>357</u>	<u>270</u>

About 80 percent of the districts containing military dependents would have received less Impact Aid under the LMI payment system in FY82 than they received from DoED. Most of the losing districts would have received zero. At first glance, it seems that the LMI payment system would hurt military dependents. However, an analysis of the losing and gaining military districts shows that the LMI payment system would benefit most military dependents.

Table 3-8 shows that the LMI payment system tends to increase payments to districts that have a substantial proportion of military dependents in relation to their total enrollment.

TABLE 3-8. MILITARY DISTRICTS THAT GAIN OR LOSE  
UNDER LMI PAYMENT SYSTEM

FY82 - \$420 Million

MILITARY ADA AS A PERCENTAGE OF TOTAL ADA	LMI LCRs (CASE #1)		DoED LCRs (CASE #2)	
	Gain	Lose	Gain	Lose
Below 5%	7%	93%	5%	95%
5.0% to 9.9%	69%	31%	17%	83%
10.0% to 19.9%	86%	14%	84%	16%
Above 20.0%	86%	14%	97%	3%

In Case #1, the LMI payment system tends to benefit those districts in which military ADA is more than 5 percent of total ADA. In Case #2, the threshold is 10 percent. The districts that receive lower payments tend to be low-impact districts. In low-impact districts, Impact Aid funds are a small proportion of the total school operating budget. Changes in Impact Aid funding for these districts have little effect on the quality of education received by federally connected students.

Not all highly impacted military districts (20 percent or more military ADA) would benefit from the LMI payment system. In Case #1, 14 percent of the

highly impacted districts lose. The LCR of these districts was reduced substantially, and they did not benefit from higher payments for Category B military dependents because their students were mostly Category A military dependents. These losing districts fare much better in Case #2, which uses DoED LCRs.

Table 3-9 demonstrates that the majority of the military dependents are in districts that would have received more Impact Aid funds under the LMI payment system than these same districts actually received in FY82. The proposed LMI payment system in Case #1 benefits 68 percent (360,000) of the military dependents and in Case #2 benefits 62 percent (327,000) of the military dependents. Although a substantial number of military dependents are in districts that would lose payments, the LMI proposal meets the test of helping far more students than are hurt.

TABLE 3-9. PROPORTION OF MILITARY DEPENDENTS  
IN GAINING AND LOSING DISTRICTS

FY82 - \$420 Million

	LMI LCRs (CASE #1)	DoED LCRs (CASE #2)
In Gaining Districts	68%	62%
In Losing Districts	32%	38%

DISTRICTS WITH INDIAN DEPENDENTS

After eliminating low-rent-housing students and Category B Federal civilian students, the Impact Aid program would continue providing funds for military dependents, Indian students, and a relatively small number of Category A dependents of Federal civilian employees. In FY82, payment was made for 96,000 Indian students. All Indian children living on Indian lands are Category A, even if their parents are employed elsewhere.



We will now examine how the LMI changes would have affected payments for Indian children and payments received by the more than 600 districts that contain some Indian children.

In FY82, 30 percent of the Impact Aid funds were paid for Indian children. As shown in Table 3-6, in Case #1, the LMI payment system also spends 30 percent of the funds for Indian children (36 percent in Case #2). The LMI payment system does not reduce the proportion of funds allocated to Indian students.

Table 3-10 shows how the LMI payment system affects districts that contain some Indian children. About one-half of these districts also contain some military dependents and/or Category A Federal civilian students.

TABLE 3-10. EFFECT OF LMI PAYMENTS ON DISTRICTS  
WITH SOME INDIAN STUDENTS

FY82 - \$420 Million

	NUMBER OF DISTRICTS <sup>a</sup>	
	LMI LCRs (Case #1)	DoED LCRs (Case #2)
Received DoED Payments	634	634
<u>LMI Payments</u>		
<u>Losing Districts</u>	<u>370</u>	<u>323</u>
Dropped	(56)	(127)
Retained but Paid Less	(314)	(196)
<u>Gaining Districts</u>	<u>264</u>	<u>311</u>

<sup>a</sup>The Indian districts that contain military dependents are also included in Table 3-7, which describes the effect on military districts.

More than one-half of the Indian districts would have received less Impact Aid under the LMI payment system than they received from DoED. Some of the losing districts would have received zero. An analysis of the losing and

gaining districts shows that the LMI payment system would benefit most Indian students.

The LMI payment system tends to increase payments to districts in which Indian students represent more than 10 percent of total enrollment, as shown in Table 3-11.

TABLE 3-11. INDIAN DISTRICTS THAT GAIN OR LOSE  
UNDER LMI PAYMENT SYSTEM

FY82 - \$420 Million

INDIAN ADA AS A PERCENTAGE OF TOTAL ADA	LMI LCRs (CASE #1)		DoED LCRs (CASE #2)	
	Gain	Lose	Gain	Lose
Below 5%	15%	85%	5%	95%
5.0% to 9.9%	32%	68%	19%	81%
10.0% to 19.9%	51%	49%	70%	30%
Above 20.0%	65%	35%	91%	9%

As shown in Table 3-12, most Indian students are located in school districts that would benefit from the proposed LMI payment system.

TABLE 3-12. PROPORTION OF INDIAN STUDENTS  
IN GAINING AND LOSING DISTRICTS

FY82 - \$420 Million

	LMI LCRs (CASE #1)	DoED LCRs (CASE #2)
In Gaining Districts	63%	81%
In Losing Districts	37%	19%

In Case #1, 63 percent of the Indian students are in gaining districts, and in Case #2, 81 percent are in gaining districts. Case #2 is clearly

preferable to Case #1 for Indian students, but this advantage is gained by shifting \$25 million from military dependents to Indian children.<sup>7</sup>

#### SUPPLEMENTARY PAYMENTS

In our April 1984 report, we recommended retention of Section 3(d)(2)(B) of P.L. 81-874. This provision states that the Secretary of Education shall increase the Impact Aid payment to a district in which 50 percent or more of the total enrollment consists of federally connected children, if the Secretary determines that the district is unable to provide an education comparable to other districts in the State, and that the district is making a reasonable tax effort.

In FY82, DoED provided a total of \$12 million in supplementary payments to the following eight districts:

- Fort Leavenworth, Kansas;
- Ayer, Massachusetts;
- City of Bellevue, Nebraska;
- North Hanover, New Jersey;
- Douglas, South Dakota;
- Dupree, South Dakota;
- Shannon, South Dakota; and
- York, Virginia.

Shannon and Dupree serve Indian children, and the other six districts serve military dependents.

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<sup>7</sup>In Case #1, 30 percent of the Impact Aid funds are allocated to Indian students; in Case #2, the allocation increases to 36 percent, with an offsetting reduction of 6 percent in the allocation for military dependents. This 6-percent differential, applied to the total FY82 Impact Aid allocation of \$420 million, results in an additional \$25 million for Indian students and a corresponding reduction for military dependents.

We examined how the LMI payment would affect the regular payments (prior to supplement) to these eight districts and the need for supplementary payments.

- For Case #1 (LMI LCRs), the regular payments are increased for seven districts and reduced for one of the districts (Shannon). The need for supplementary payments is reduced from \$12.0 million to \$8.3 million. Two of the eight districts (City of Bellevue and North Hanover) would not need any supplementary payments.
- For Case #2 (DoED LCRs), the regular payments are increased for seven of the districts and reduced for one district (City of Bellevue). The need for supplementary payments is reduced from \$12.0 million to \$9.4 million.

Although the LMI payment system would reduce the need for supplementary payments for seven out of the eight districts receiving such payments in FY82, it may create a need for supplementary payments in other districts. Additional high-impact districts would probably qualify for Section 3(d)(2)(B) payments in Case #1 of the LMI payment system, because of LCR reductions. For example, in Case #1 the regular payments for Fort Sam Houston, Randolph Air Force Base (AFB), and Lackland AFB are reduced by a total of \$1.2 million, a 32-percent reduction from the payments actually received by these districts in FY82. Nearly all of the students in these districts are Category A military dependents. The reduction in regular payments caused by the Case #1 LCR-computation method might qualify these districts for supplementary payments. Other heavily impacted districts serving Indian students might also be eligible for supplementary payments under Case #1. We do not think that Case #2 would increase the number of districts eligible for supplementary payments.

It is impossible to design an allocation system for Impact Aid that results in equity for all districts. There is too much variation among districts in terms of their operating costs and the financial resources they derive from local taxes and from State aid. The best that can be done is to

design an allocation method that can function rationally within the bounds of the funds that are likely to be available for Impact Aid, that is equitable for most districts, and that provides a special review for highly impacted districts hurt by the regular allocations.

Section 3(d)(2)(B) provides the necessary safety net for highly impacted districts and should be used to a greater extent than it has been in the past. Overall costs can be reduced by a payment system that is frugal in making payments to most districts but gives all districts meeting the initial 50-percent criterion a fair and open opportunity for supplementary payments. We have not evaluated the DoED procedures for handling Section 3(d)(2)(B) applications. We have talked to school administrators. They either distrust the evaluation process or say that it is a complete mystery to them. Unless this perception is changed, high-impact districts will resist changes to the Impact Aid allocation system that would reduce the regular allocation to their district and make them dependent on the Section 3(d)(2)(B) process for supplementary payments.

The implementation of the changes we propose to the Impact Aid program -- especially Case #1, which reduces LCRs -- requires the use of an equitable supplementary payment process that is understood by highly impacted districts.

#### CASE #1 VERSUS CASE #2

In both Case #1 and Case #2, we tested the combined effect of changing the types of children eligible for Impact Aid, revising the entitlement weights, and using the absorption-rate mechanism. In Case #1, we also revised the method for determining LCRs, while in Case #2 we used the old DoED LCRs.

After examining the test results, we conclude that the Case #1 proposal is better than Case #2, for the following reasons:

1. Case #1 achieves a more equitable balance between funds for military dependents and funds for Indian children.

Case #2 provides \$25 million less to military dependents than does Case #1 and reduces the funds available to districts serving military dependents by a like amount. These funds are needed by these districts to offset the losses caused by the elimination of funds for Category B Federal employee dependents and low-rent-housing children. In Case #2, the total funding allocated to districts serving military dependents is 6 percent less than actually received by these districts from DoED in FY82, but Indian districts would experience a 15-percent increase. In Case #1, the total funds allocated to districts serving military dependents and to districts serving Indian children are both marginally higher than the actual DoED allocation.<sup>8</sup>

2. Case #1 eliminates fewer districts than Case #2.

Case #2 drops more districts, because, by using higher LCRs, it generates a higher full-entitlement level and therefore requires the application of a higher absorption rate to reduce payments to the actual funding level. Starting with 2,193 districts paid by DoED in FY82, Case #1 makes zero payments to 1,178 of these districts; Case #2 makes zero payments to 1,396 districts. Most of the additional districts dropped in Case #2 are districts serving military dependents.

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<sup>8</sup> 1.8 percent higher for military districts and 1.3 percent higher for Indian districts. These increases came from funds lost by districts that contained low-rent-housing students and/or Federal civilian Category B students but no military dependents or Indian students.

#### 4. EVALUATION AND IMPLEMENTATION

This chapter evaluates the results of the test against the objectives established in the April 1984 LMI report. It then discusses implementation of the proposed changes to the Impact Aid program.

##### ATTAINMENT OF OBJECTIVES

The April 1984 report established three objectives for an improved payment system. The evaluation will assume that the LMI Case #1 proposals are adopted.

Objective #1: Provide more Impact Aid funds or an equitable share of available funds to school districts serving military dependents.

This objective is achieved substantially, as demonstrated by the following test results:

- Sixty-eight percent of the military-dependent students are in districts that would receive higher aid payments under the LMI payment system.
- Thirty-two percent of the military dependents are in districts that would receive either lower payments or none at all. These districts tend to have a low proportion of military-dependent students -- less than five percent of their total enrollment.
- Some of the losing military districts that are very heavily impacted with military dependents may be eligible for supplementary payments.

Objective #2: Improve the method used to allocate Impact Aid when funds are short.

This objective is achieved by the absorption-rate mechanism we proposed and tested. When available funds are less than required to pay at the full-entitlement level, the new method makes zero payments to the most lightly impacted districts and reduces payments to remaining districts in proportion to their ratio of federally connected students to total enrollment. The sharp distinction between payments to regular districts and to Super districts is

eliminated and replaced by a payment system favoring more heavily impacted districts on a smooth, graduated scale.

Objective #3: Simplify a payment system that has become overly complicated.

The proposed changes result in the following improvements that simplify the management of the program:

- The LCRs for each district can be computed in a few hours using data published by the National Center for Educational Statistics, an organizational element of DoED.
- The 15 types of federally connected students are reduced to 7 types.
- When funds are not sufficient to pay at the full-entitlement level, the LMI absorption rate would reduce the number of districts eligible for payment. For example, the number of districts paid would have been reduced by 53 percent in FY82, the test year. This reduction should ease the administrative burden in DoED.
- The absorption-rate mechanism provides a high-speed method for determining the allocation of Impact Aid funds by district and for examining the effect of alternative funding levels on district allocations.
- The cost of full entitlement would be reduced to a more realistic amount. A smaller gap between full entitlement and actual funding makes the allocation of funds to districts less controversial.

The LMI proposal does add one additional administrative burden. Currently, districts with a Federal student ADA that is less than 3 percent of their total ADA do not apply for Impact Aid unless they have 400 or more federally connected students. The LMI proposal would permit all districts that educate military dependents, Indian children, and Category A Federal civilian children to apply for Impact Aid on the assumption that they might receive payments if funds are available to pay at the full-entitlement level. If sufficient funds are not available, most of these districts would receive zero payments when the absorption rate is applied.<sup>1</sup> To reduce the number of

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<sup>1</sup>We are unable to estimate the number of very-low-impact districts that are currently excluded from applying by the 3-percent eligibility rule, because these districts are not in the DoED data base.



hopeless applications, we now believe it would be desirable to continue having a minimum-eligibility rule. We suggest excluding districts that have a weighted Federal ADA of less than 0.5 percent of their total ADA.<sup>2</sup>

#### IMPLEMENTATION

It will be difficult to get both the Executive Branch and Congress to approve the package of changes recommended by LMI because:

- LMI recommends eliminating payments for Category A and B low-rent-housing students and for the Category B children of Federal civilian employees. The Impact Aid budgets submitted by the Executive Branch from FY82 to FY86 have proposed the elimination of payments for all Category B students, including Category B military dependents. Congress, on the other hand, has continued to authorize and fund payments for all types of Category B students.
- When there is not enough money to pay at the full-entitlement level, the LMI payment system protects the highly impacted districts and makes zero or low payments to low-impact districts. Congress prefers an allocation plan that spreads the funds over a large number of districts.

Although it will be difficult to achieve agreement on the changes we propose, we believe that the effort should be made. To do nothing risks the elimination of all Impact Aid funds for Category B military dependents. On the basis of the test we conducted, we recommend that DoD seek adoption of the proposed changes to the Impact Aid program.

Others may be able to improve on the proposals we tested. We advise DoD to conduct a test of any alternative proposals before agreeing to their adoption.

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<sup>2</sup>Raising the eligibility cut-off point to 1.0 percent or 2.0 percent would eliminate many more districts from applying but risks depriving some districts from receiving Impact Aid in years when the funds available for Impact Aid are close to full entitlement. For FY85, we estimate that an absorption rate of 0.8 percent would be used if the LMI payment system were in effect.

APPENDIX A

EXECUTIVE SUMMARY

PROPOSAL TO REVISE THE FEDERAL IMPACT AID PROGRAM

LMI TASK ML326



## Executive Summary

### PROPOSAL TO REVISE THE FEDERAL IMPACT AID PROGRAM

School Assistance for Federally Affected Areas (Impact Aid) helps compensate local school districts for the expense of educating federally connected children, including:

- children of Federal civil servants;
- children of military personnel;
- children who live in public housing and
- children who live on Indian lands.

The rationale for Impact Aid is that school enrollments and educational costs are increased by the presence of Federal activities, but Federal property cannot be taxed. The Department of Education (DoED) administers the Impact Aid Program.

As a result of reductions in Impact Aid funding starting in Fiscal Year 1982, some school districts have attempted to collect tuition from military parents, and other districts have changed or are planning to change their boundaries to avoid the responsibility of educating military dependents. These actions by local school districts are a symptom of the financial problems in many school districts serving military installations.

The law defines two broad categories of federally connected children. The parents of Category A children live and work on Federal property. The parents of Category B children live or work on Federal property, but not both. Most of the Impact Aid budget reduction since 1982 has been achieved by reducing the payments to local school districts for all Category B children to token amounts. About 60 percent of the military dependents included in the

Impact Aid Program are Category B children (i.e., the military parent is assigned to a military installation but lives in a local community).

The single most important Department of Defense (DoD) Impact Aid objective should be the restoration of adequate funding for military-dependent Category B children, while not reducing payments for Category A military dependents. Although there is a good case for eliminating aid for the Category B children of Federal civilian employees and for children who live in public housing, there is sound justification for payments for military-dependent Category B children. Military personnel who live off base do pay local property taxes (as home owners or renters), however, military personnel have tax benefits that deprive local and State governments of significant amounts of tax revenue:

- Purchases in commissaries, post exchanges, military clubs and package liquor stores are exempt from sales taxes, cigarette taxes and alcohol taxes.
- Quarters and subsistence allowances are exempt from State income taxes.
- Military personnel usually do not pay income and personal property taxes in the States where they are stationed.

We recommend changes to the methods currently used to calculate the Impact Aid payments for each impacted school district. The objectives of those changes are to:

- provide more Impact Aid funds to school districts serving military dependents, or an equitable share of available funds;
- improve the formulas used to give priority to more heavily impacted school districts and
- simplify a payment system that has become overly complicated.

To achieve these objectives we recommend the following changes to the payment system:

- Eliminate Impact Aid payments for low-rent-housing Categories A and B children and for the Category B dependents of Federal civilian employees.

- Raise the per-pupil payments for military-dependent Category B children to the full-entitlement level authorized in Fiscal Year 1981.
- Revise the current methods for computing per-pupil costs raised from local revenue (Local Contribution Rate) to simplify the process and to reduce the Local Contribution Rate for some districts.
- Change the method used for adjusting payments when Impact Aid funds are reduced or raised. Under the current system, when Impact Aid funds are inadequate to make payments at the full-entitlement level, the per-pupil payments are reduced for some types of children and for children in less heavily impacted districts. We recommend that all payments be made at full-entitlement level. Fund shortages should be accommodated by requiring all districts to absorb portions of their federally connected children without payment. The absorption rate can be revised each year to adjust to changes in funding levels. This recommendation will prevent the erosion of the full-entitlement price authorized for each type of child, including the price for military-dependent Category B children.
- Change the method used to favor more heavily impacted districts. The current method provides much higher per-pupil payments to Super A and Super B districts<sup>1</sup> than to regular districts. The sharp distinction between regular and Super districts should be replaced by a method that rewards more heavily impacted districts on a graduated scale.

Before DoD recommends these system changes to DoED, it would be prudent to test, by use of computer simulations, how these changes would affect payments to individual school districts.

Two other issues are likely to be considered by the Administration in proposing revisions to the Impact Aid legislation.

The first issue is: "Should the current Federal-to-local payment system be changed to a Federal-to-State payment system?" A Federal-to-State payment system would simplify administration at the Federal level and involve State governments in the allocation of Impact Aid funds. State governments have better information on the wealth, the tax effort and the relative financial needs of all their districts. However, State and local education agencies do

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<sup>1</sup>In a Super A district, 20 percent or more of the district's total enrollment is composed of Category A federally connected children. In a Super B district, 20 percent or more of the district's total enrollment is composed of Category B federally connected children.

not exhibit much enthusiasm for a Federal-to-State payment system. School districts fear that their State governments would not allocate the funds fairly. The State governments feel that aid to impacted districts is a Federal problem. We recommend that DoD request DoED to sponsor discussions on this issue with a sample of State and local education agencies to ascertain whether such attitudes can be changed.

The second issue is: "Should Impact Aid responsibility for military dependents be transferred from DoED to DoD?" If the funds currently budgeted by DoED were transferred to DoD, the main cost to DoD would be the funds it decided to add to enhance the program. The transfer of responsibility is the only sure way to increase Impact Aid funds for military dependents. We recommend that DoD propose the transfer of Impact Aid funding for military dependents from DoED to DoD. However, since the Administration or Congress may oppose the transfer, DoD should concurrently propose reforms to the Impact Aid legislation, on the assumption that DoED is likely to continue to manage the entire Impact Aid Program.

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APPENDIX B

FY82 LOCAL CONTRIBUTION RATES - DoED COMPARED TO LMI

TABLE B-1. FY82 LOCAL CONTRIBUTION RATES - DoED COMPARED TO LMI

STATE	DoED LCRs	LMI LCRs	PERCENT CHANGE (WEIGHTED)
Alabama	\$1,084	\$ 708	-35.3%
Alaska	2,274 - 4,548	2,144	-11.1
Arizona	1,084 - 3,022	970	-23.4
Arkansas	1,084	656	-39.9
California	1,084 - 3,417	1,013	-9.3
Colorado	1,176 - 2,574	1,281	-0.5
Connecticut	1,171 - 2,400	1,603	-6.5
Delaware	1,237 - 1,361	1,253	-7.9
District of Columbia	1,535	2,542	+65.6
Florida	1,084	838	-22.7
Georgia	*1,055 - 1,084	698	-35.8
Hawaii	1,120	983	-12.3
Idaho	1,084	750	-31.0
Illinois	1,160 - 2,016	1,387	+9.3
Indiana	*959 - 1,084	876	-19.1
Iowa	*1,116 - 1,126	1,278	+13.5
Kansas	*1,055 - 1,146	1,114	+0.3
Kentucky	*1,055 - 1,084	714	-35.4
Louisiana	1,084	766	-29.4
Maine	1,084	824	-24.4
Maryland	1,084 - 1,816	1,372	-13.6
Massachusetts	1,350 - 2,979	1,686	+5.4
Michigan	1,270 - 2,308	1,407	+5.4
Minnesota	1,084 - 1,150	1,156	+0.9
Mississippi	1,084	623	-43.1
Missouri	1,084 - 1,366	1,026	-8.1
Montana	1,183 - 5,033	1,113	-42.4
Nebraska	1,084 - 3,899	1,628	+18.9
Nevada	1,084	975	-10.1
New Hampshire	1,084 - 1,826	1,631	-2.6
New Jersey	1,591 - 2,088	1,825	+10.0
New Mexico	*1,055 - 1,084	849	-21.6
New York	1,652 - 9,971	1,863	+1.9
North Carolina	1,084	756	-30.4
North Dakota	1,084	861	-20.6
Ohio	1,084 - 1,912	965	-18.0
Oklahoma	1,084	828	-23.8
Oregon	1,084 - 1,288	1,529	+19.3
Pennsylvania	1,215 - 2,598	1,242	-1.4
Rhode Island	1,224 - 1,536	1,483	+1.8
South Carolina	*1,055 - 1,084	719	-33.6
South Dakota	1,084 - 1,707	1,175	-18.6
Tennessee	*780 - 1,084	693	-37.1
Texas	1,084 - 1,650	847	-25.6
Utah	1,084	758	-30.3
Vermont	1,084	1,281	+18.1
Virginia	1,084 - 2,737	973	-30.4
Washington	1,245	1,168	-6.2
West Virginia	1,084	853	-23.4
Wisconsin	1,406 - 1,974	1,422	-2.7
Wyoming	1,084 - 3,259	1,521	-8.2
TOTAL	\$780 - \$9,971	\$623 - \$2,542	-17.0%

\* These LCRs are probably data-base errors. In FY82, \$1,084 was the minimum LCR amount, based on one-half of the national average educational cost. The data base shows LCRs lower than \$1,084 for a few districts.



APPENDIX C

LMI PAYMENTS COMPARED TO DoED PAYMENTS  
BY STATE, PERCENTAGE CHANGE

FY82 - \$420 Million

TABLE C-1. LMI PAYMENTS COMPARED TO DoED PAYMENTS  
BY STATE, PERCENTAGE CHANGE

FY82 - \$420 Million

STATE	USING LMI LCRs (CASE #1)	USING DoED LCRs (CASE #2)	STATE	USING LMI LCRs (CASE #1)	USING DoED LCRs (CASE #2)
Alabama	-42.4%	-55.9%	Montana	-3.3%	+62.2%
Alaska	+18.5	+27.3	Nebraska	+13.1	+15.5
Arizona	-3.3	+18.0	Nevada	-0.5	-56.7
Arkansas	-15.7	+2.4	New Hampshire	+12.5	+8.5
California	+15.6	+3.6	New Jersey	+16.4	+1.4
Colorado	+42.7	+4.3	New Mexico	-0.9	+14.8
Connecticut	+1.1	-0.6	New York	-50.6	-65.5
Delaware	+121.6	-31.2	North Carolina	+14.5	+29.5
District of Columbia	-100.0	-100.0	North Dakota	+8.9	+28.5
Florida	-13.8	-34.7	Ohio	-17.1	-21.2
Georgia	-34.7	-40.3	Oklahoma	-1.5	+7.0
Hawaii	+17.5	+3.9	Oregon	-4.1	-35.5
Idaho	-28.4	-11.8	Pennsylvania	-75.6	-89.4
Illinois	+13.1	-6.4	Rhode Island	+14.2	-4.3
Indiana	-12.1	-9.0	South Carolina	+3.2	+13.9
Iowa	-26.9	-48.7	South Dakota	+1.4	+7.9
Kansas	+23.0	+16.6	Tennessee	-51.5	-52.6
Kentucky	-35.1	-47.2	Texas	+3.8	+12.5
Louisiana	-2.6	+15.2	Utah	-47.0	-48.0
Maine	-1.3	+16.1	Vermont	-100.0	-100.0
Maryland	-28.0	-66.7	Virginia	+32.4	+37.4
Massachusetts	-20.3	-25.4	Washington	+23.6	+13.4
Michigan	+23.7	+4.4	West Virginia	-86.1	-100.0
Minnesota	-0.7	-16.3	Wisconsin	+2.0	-9.8
Mississippi	-25.7	-5.1	Wyoming	-15.2	-13.2
Missouri	+12.7	+14.6			

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20. ABSTRACT (Continue on reverse side if necessary and identify by block number) School Assistance for Federally Affected Areas (Impact Aid) helps compensate local school districts for the expense of educating federally connected children. An April 1984 LMI report "Proposal to Revise the Federal Impact Aid Program" (Task ML326) proposed changes that address: (1) the types of children eligible for Impact Aid; (2) the method used to compute the Local Contribution Rate; (3) the entitlement weight by type of child; and (4) the allocation method used to adjust to different levels of program funding.			

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